

## CEPS POLICY BRIEF



Thinking ahead for Europe

# Paving the Way for Micro-, Small- and Medium-Sized Enterprises in the Southern Mediterranean

**Rym Ayadi and Willem Pieter De Groen****No. 314, 14 January 2014**

*The Arab Spring, which took root in Tunisia and Egypt in the beginning of 2011 and gradually spread to other countries in the southern Mediterranean, highlighted the importance of private-sector development, job creation, improved governance and a more equitable distribution of economic opportunities. The developments led to domestic and international demands on the governments in the region to implement the reforms needed to enhance business and investment conditions, modernise their economies and support the development of enterprises.*

*Central to these demands are calls to enhance the growth prospects of micro-, small- and medium-sized enterprises (MSMEs), which carry out an overwhelming majority of the region's economic activity. A comprehensive survey among circa 600 high-growth potential MSMEs in Algeria, Egypt, Morocco and Tunisia identified and ranked the key obstacles impeding high-growth potential MSMEs. This Policy Brief summarises the main results and policy recommendations that can be drawn from this survey, which has been analysed in depth by Ayadi & De Groen (2014). The survey is available for downloading from the [CEPS website](http://www.ceps.eu).*

Notwithstanding their essential contribution to innovation, job creation and local development, MSMEs across the southern Mediterranean are confronted with a number of problems that hamper their growth. Ayadi & De Groen (2014) assessed what is required to unlock the growth potential of the most promising MSMEs. Based on a thorough literature review and inputs from economic experts from the countries under

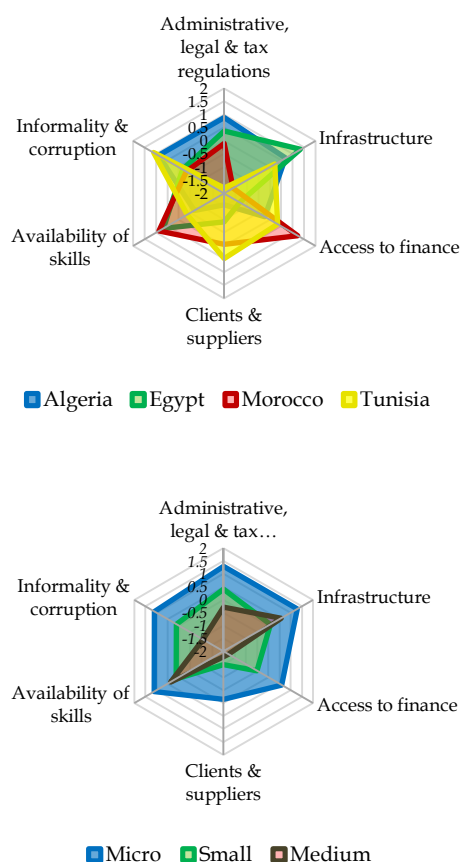
investigation, a questionnaire was designed to identify the problems that confront MSMEs with high-growth potential. Six areas were identified as key potential obstacles that could hinder MSME development: administrative, legal and tax regulations; infrastructure (communications, utility services, roads and transport); access to financial instruments; clients and suppliers; availability of skills; and informality and corruption (see Figure 1).

Rym Ayadi is Senior Research Fellow and Willem Pieter De Groen is Researcher at the Centre for European Policy Studies. This Policy Brief presents the policy findings of a larger study (Ayadi & De Groen, 2014) funded by FEMISE (Forum Euroméditerranéen des Instituts de Sciences Économiques) a Euro-Mediterranean network consisting of more than 80 economic research institutes, representing the 37 partners of the Barcelona Process.

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Figure 1. Comparison of obstacles faced by MSMEs in the southern Mediterranean, by country and by size



*Note:* The figures above show the number of standard deviations from the mean. The averages are calculated differently for each figure to show where the differences are most apparent. For the left-hand figure, the country means are used, whereas for the right-hand figure the benchmark is formed by the total sample mean. A higher score indicates that the area is perceived as a relatively more severe obstacle.

*Source:* Ayadi & De Groen (2014).

Overall, the survey responses suggest that the difficulties in dealing with all of these obstacles are more or less comparable, with the exception of infrastructure, which is widely considered more difficult as it far beyond the control of MSMEs (see also Figure 1). Turning to the individual countries, MSMEs in Algeria have the most difficulties with infrastructure availability, informality and corruption as well as administrative, legal & tax regulations. In Egypt MSMEs also face the most difficulties

with the availability of sound infrastructure, followed by administrative, legal and tax regulations and the availability of skilled workers. Morocco is the only country in the region where infrastructure is considered the least problematic, but its MSMEs report experiencing the most difficulties in obtaining access to finance and skilled workers. In Tunisia, MSMEs experience severe difficulties in all six categories, with relatively the most difficulties with informality and corruption and fewer difficulties complying with administrative, legal and tax regulations.

Policy-makers in the four countries have attempted to respond to the challenges facing MSMEs, since they are essential for innovation, job creation and local development. All countries have set up national SME agencies to support this segment of companies. The majority of the MSMEs in the sample seem to benefit from services provided by SME support organisations, but it is not certain that these agencies are effective in tackling the key obstacles to MSME development.

Based on the survey findings summarised in the table in Annex 1, the following policy measures could help policy-makers in Algeria, Egypt, Morocco and Tunisia to attenuate the impacts of these obstacles in their countries:

*To deal with administrative, legal and tax regulations:*

- Assess the extent of administrative and regulatory burdens from an MSME perspective and consider simplifying procedures for enterprise registration and adjusting certification and trademark procedures and tax, import/export/foreign investment regulations proportionately to ensure that MSMEs can benefit at all stages of their development.
- Further enable MSME agencies to support the companies of different sizes

and activities to comply effectively with the administrative, legal and tax regulations.

*To tackle corruption and informality:*

- Standardise the procedures for public procurement and ensure that the procedures are publicly disclosed and are fully transparent.
- Provide incentive schemes (e.g. subsidies and tax holidays) for the informal sector to become more formalised.
- Simplify labour regulations to facilitate hiring of staff with different levels of competences.

*To improve the infrastructure necessary for MSMEs to prosper:*

- Promote private-public partnership infrastructure projects (e.g. road infrastructure, electricity, water infrastructure, sanitation, etc.) at both national and local/regional levels and facilitate the procedures for MSMEs to participate in such projects.
- Privatised and liberalised communications and internet companies as well as markets to improve the efficiency, quality and availability in these sectors.

*To promote access to finance at all stages of MSME development:*

- Design finance sources for MSMEs at all stages of their development:
  - For micro-enterprises, secure finance through the development of microfinance institutions and new microfinance products;
  - For small- to medium-sized enterprises, improve the equity base through support to investment funds/risk capital and to pilot funds for small enterprises;
  - Support specific segments, such as start-ups through start-up funds, industrial/technology clusters and women-owned enterprises and

increasing the volume and outreach of financing instruments such as leasing and factoring, export/import credit and guarantee schemes; and,

- Increase the access to finance for MSMEs through a support to guarantee institutions and the creation of a counter-guarantee fund to cover risk-sharing in particular for exporting companies.
- Enhance capacity-building for micro- and small start-ups and technology/innovative ventures, entrepreneurs and also local entities providing technical, business and financial support services to MSMEs. Such support should include training on how to build a credible business plan, maintain a balance sheet and collect and present reliable credit information, all of which are essential steps to be granted a loan or an overdraft.
- Support training of finance professionals dealing with MSMEs e.g. by 'pairing' European banks' financial experts with their southern Mediterranean counterparts to share best practices.
- Promote the development of national credit bureaus with a specific focus on MSMEs in a first stage and a regional credit bureau network to provide cross-border information to support risk-management approaches, particularly when MSMEs envisage clustering in production value chains and/or accumulating origin to preferentially export to target markets (e.g. using the AGADIR agreement<sup>1</sup>).
- Support capacity-building actions aimed at enhancing reliable, transparent and comparable MSME financial reporting. The lack of reliable accounting data is

<sup>1</sup> The Agadir Agreement (Agreement Establishing a Free Trade Area amongst Arab Euro-Mediterranean Countries) was signed in 2004 by Jordan, Tunisia, Egypt and Morocco to establish a free trade area among the four countries.

among the main reasons why MSMEs have poor access to banking credit. The availability of reliable, transparent and comparable financial information would enhance MSMEs' access to finance and cross-border investments.

*To promote the availability of skilled workers:*

- Support the design of new more business-oriented curricula that promote critical thinking, problem-solving and leadership necessary for private-sector development;
- Develop public-private partnerships aimed at promoting apprenticeship or mentoring programmes to improve work-related skills; and
- Develop joint programmes with universities and technical institutes with key players in the MSMEs and supported by the government.

*To facilitate availability of clients and suppliers:*

- Undertake comprehensive impact assessments on the import/export market to ensure that local competition is fair;
- Develop more effective business clusters and expanding the existing ones to allow micro enterprises in particular to overcome their size obstacles and to enhance joint capacity-building between different MSMEs;
- Empower local MSME support organisations, such as the MSME development agencies, to promote the MSMEs in both the domestic market and in the international market; and
- Promote international business-to-business forums to enhance foreign market access for MSMEs.

To tackle these obstacles, countries are recommended to develop national strategies that target MSMEs. Such a strategy has to cover all aspects that contribute to national economic development, from trade, industrial development, education, and

R&D to regional and sectoral development, as well as finance.

Beyond national MSME policies, it is essential to strengthen the regional cooperation in the area of MSMEs starting from an evaluation of the lessons learned from monitoring progress in the implementation of the Euro-Med Charter for Enterprise<sup>2</sup> and from an understanding of its limitations, in terms of the policy framework and availability of resources. To this end, Ayadi & Fanelli (2011) have provided a comprehensive proposal for a blueprint to develop regional cooperation in the area of MSMEs.

In the final analysis, it remains to be seen the extent to which the recommended policy measures would address the obstacles for MSMEs. There is also a question, however, of whether these measures will contribute to further economic growth and local development. Hence, the aim of the survey has been to identify the obstacles hindering MSME development and to assess the relative importance of these obstacles and to a lesser extent the benefits that their removal would generate.

To allow policy-makers to take balanced and informed decisions, it is highly recommended to perform ex-ante impact assessments to estimate both the expected economic costs and benefits of such policy measures and to continue monitoring the development of the MSME sector. At a later stage ex-post impact assessment are recommended to assess whether the chosen policy measures have produced the desired impacts and if not, to implement prompt corrective actions.

<sup>2</sup> The Euro-Mediterranean Charter for Enterprise aims to set out the principles for governments to create an environment conducive to investment and private-sector development. See the European Commission website for the complete text ([http://ec.europa.eu/enterprise/policies/international/files/charter\\_11\\_dimensions\\_en.pdf](http://ec.europa.eu/enterprise/policies/international/files/charter_11_dimensions_en.pdf)).

## References

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## Annex 1. Most severe problems within each obstacle (average degree of difficulty), by country and by size of enterprise

	Algeria		Egypt		Morocco		Tunisia		Micro		Small		Medium	
<b>1</b>	<b>Informality &amp; corruption</b>	<b>32</b>	<b>Infrastructure</b>	<b>33</b>	<b>Access to finance</b>	<b>33</b>	<b>Informality &amp; corruption</b>	<b>9</b>	<b>Administrative, legal &amp; tax regulations</b>	<b>34</b>	<b>Administrative, legal &amp; tax regulations</b>	<b>41</b>	<b>Infrastructure</b>	<b>40</b>
	Labour costs associated with hiring formal employees	30	Electricity: Outages	34	Overdraft facility	33	Informal gifts to accomplish simple administrative tasks	21	Foreign investment regulations	19	Import and export regulations	42	Electricity: Outages	44
	Informal gifts to accomplish simple administrative tasks	32	Electricity: Frequency variations	56	Bank loan	34	Labour costs associated with hiring formal employees	25	Labour regulations	38	Public procurement procedures	44	Roads & transport: Quality	56
	Informal gifts to secure government contracts	36	Roads & transport: Quality	60	Non-bank loan	42	Informal gifts to secure government contracts	26	Import and export regulations	42	Quality standards & certification	44	Electricity: Frequency variations	58
<b>2</b>	<b>Administrative, legal &amp; tax regulations</b>	<b>32</b>	<b>Availability of skills</b>	<b>41</b>	<b>Availability of skills</b>	<b>37</b>	<b>Clients &amp; suppliers</b>	<b>13</b>	<b>Infrastructure</b>	<b>34</b>	<b>Availability of skills</b>	<b>43</b>	<b>Availability of skills</b>	<b>41</b>
	Quality standards & certification	11	Relevance of curricula taught at school	38	Availability of leadership skills	21	Competition from imports	17	Electricity: Outages	33	Availability of leadership skills	38	Relevance of curricula taught at school	38
	Registering a copyright/trademark	19	Availability of other job-related skills	45	Availability of problem solving skills	29	Access to export credit	21	Electricity: Frequency variations	46	Relevance of curricula taught at school	38	Availability of other job-related skills	46
			Availability of numerical & technical skills	50	Availability of critical thinking skills	30	Lower foreign demand	21	Roads & transport: Access to ports	56	Poaching of skilled workers by other employers	46	Availability of leadership skills	46
<b>3</b>	<b>Infrastructure</b>	<b>34</b>	<b>Administrative, legal &amp; tax regulations</b>	<b>44</b>	<b>Clients &amp; suppliers</b>	<b>47</b>	<b>Access to finance</b>	<b>13</b>	<b>Availability of skills</b>	<b>35</b>	<b>Informality &amp; corruption</b>	<b>43</b>	<b>Administrative, legal &amp; tax regulations</b>	<b>46</b>
	Water: Outages	35	Tax regulations	50	Competition from imports	33			Relevance of curricula taught at school	37	Competition with unregistered enterprises	40	Import and export regulations	52
	Water: Access to clean water	41	Foreign investment regulations	57	Access to import credit	36			Availability of critical thinking skills	38	Labour costs associated with hiring formal employees	41	Tax regulations	52
	Internet: Slow speed	42	Import and export regulations	57					Poaching of skilled workers by other employers	42	Informal gifts to accomplish simple administrative tasks	43	Labour regulations	54

## Annex 1. (cont.)

Algeria			Egypt			Morocco			Tunisia			Micro			Small			Medium		
4	Access to finance	44	Informality & corruption	51	Administrative, legal & tax regulations	48	Infrastructure	14	Informality & corruption	35	Infrastructure	43	Informality & corruption	53						
	Bank loan	30	Competition with unregistered enterprises	46	Labour regulations	35	Internet: Slow speed	9	Informal gifts to accomplish simple admin tasks	34	Electricity: Outages	43	Competition with unregistered enterprises	52						
	Overdraft facility	39	Informal gifts to accomplish simple administrative tasks	52	Tax regulations	42	Internet: Access to broadband	13	Labour costs associated with hiring formal employees	34	Electricity: Frequency variations	53	Informal gifts to accomplish simple administrative tasks	56						
	Savings account	46			Public procurement procedures	43	Internet: Setting up website	20	Competition with unregistered enterprises	34	Internet: Slow speed	53								
5	Availability of skills	49	Clients & suppliers	59	Informality & corruption	50	Availability of skills	17	Access to finance	39	Access to finance	48	Access to finance	58						
	Availability of leadership skills	30	Variability of domestic demand	32	Labour costs associated with hiring formal employees	35	Availability of critical thinking skills	11	Overdraft facility	37	Bank loan	35	Bank loan	41						
	Availability of problem solving skills	42	Lower domestic demand	33	Competition with unregistered enterprises	43	Relevance of curricula taught at school	18	Bank loan	42	Overdraft facility	35	Overdraft facility	47						
	Relevance of curricula taught at school	42	Variability of foreign demand	34	Informal gifts to secure government contracts	47	Availability of problem solving skills	19	Export credit facility	44	Import credit facility	49	Non-bank loan	63						
6	Clients & suppliers	58	Access to finance	64	Infrastructure	65	Administrative, legal & tax regulations	25	Clients & suppliers	45	Clients & suppliers	56	Clients & suppliers	58						
	Late or incomplete payments for products delivered	33	Bank loan	46	Internet: Slow speed	46	Import and export regulations	17	Late or incomplete payments for products delivered	22	Variability of foreign demand	33	Lower domestic demand	38						
	Variability of foreign demand	40	Overdraft facility	50	Internet: Outages	47	Foreign investment regulations	21	Lower foreign demand	25	Lower foreign demand	34	Variability of domestic demand	39						
	Access to export credit	40	Non-bank loan	59	Internet: Access to broadband	49	Tax regulations	22			Competition from imports	42	Variability of foreign demand	39						

Note: The table shows the most severe problems encountered within each obstacle by country and size of enterprise. The respondents were asked to rate the different problems. The resulting scores have been averaged and converted into a scale of 0 to 100, with 0 being the most-, 50 moderately- and 100 being the least-difficult.

Source: Ayadi & De Groen (2014).